

**LEGISLATIVE SERVICES AGENCY  
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

200 W. Washington, Suite 301  
Indianapolis, IN 46204  
(317) 233-0696  
<http://www.in.gov/legislative>

**FISCAL IMPACT STATEMENT**

**LS 6095**

**BILL NUMBER:** SB 39

**NOTE PREPARED:** Oct 15, 2010

**BILL AMENDED:**

**SUBJECT:** Taxation of Civil Service Annuities.

**FIRST AUTHOR:** Sen. Landske

**FIRST SPONSOR:**

**BILL STATUS:** As Introduced

**FUNDS AFFECTED:** X GENERAL  
DEDICATED  
FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** This bill increases the federal civil service annuity state income tax deduction from \$2,000 to \$10,000 over a multi-year phase-in period beginning in 2012. It provides that the deduction is available to a surviving spouse.

**Effective Date:** January 1, 2012.

**Explanation of State Expenditures:** *Department of State Revenue (DOR):* The DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to reflect the 7-year phase-in of the increase from \$2,000 to \$10,000 for the income tax deduction for civil service annuities. The DOR's current level of resources should be sufficient to implement the change.

**Explanation of State Revenues:** *Summary* - The bill would reduce Adjusted Gross Income (AGI) Tax liabilities of individual taxpayers who receive federal civil service retirement benefits and currently claim the deduction for this income. The bill phases in an increase in the deduction from \$2,000 to \$10,000 over seven years. The potential revenue loss due to the increase in the deduction is summarized in the table below.

<b>Tax Year</b>	<b>Fiscal Year</b>	<b>Maximum Deduction</b>	<b>Estimated Annual Revenue Loss</b>
2012 and 2013	2013 and 2014	\$4,000	\$205,000
2014 and 2015	2015 and 2016	\$6,000	\$400,000
2016 and 2017	2017 and 2018	\$8,000	\$585,000
2018 and after	2019 and after	\$10,000	\$760,000

The fiscal year impact of the deduction increase would begin in FY 2013. If recent trends persist, the annual revenue loss after the phase-in is complete could potentially decline by about 1.3%. The impact of extending the deduction to a surviving spouse could potentially increase the revenue loss from the bill, but the extent of the impact is unknown.

**Background Information** - Under current statute, taxpayers may deduct up to \$2,000 in civil service annuity income. The deduction is equal to the difference between \$2,000 and the total amount of social security and railroad benefits received by the taxpayer. State tax return data indicates that 4,159 taxpayers deducted approximately \$7.1 M in civil service annuity pay from AGI in 2008. This amount resulted in a revenue loss of about \$240,000. From 2003 to 2008, this deduction declined by an average of 1.3% per year. Data from the U.S. Office of Personnel Management indicates that there were about 25,000 federal retirees and about 8,000 surviving spouses of federal retirees residing in Indiana in 2009. These individuals received \$855 M in civil service annuity payments during 2009, with the average annuity to retirees equal to about \$27,000. The average survivor's benefit was about \$15,000.

It is assumed that taxpayers currently claiming the maximum deduction do not receive social security or railroad retirement benefits. Based on the average benefits cited above, it is also assumed that these taxpayers would be able to claim the maximum deductions established in the bill. In 2008, 3,174 taxpayers claimed the maximum deduction, with 73 claiming a \$4,000 deduction on joint returns. This total has declined by about 1.1% annually since 2000.

The bill increases the deduction beginning in tax year 2012, thus, the fiscal impact of the phase-in will commence in FY 2013. Revenue from the AGI tax on individuals is distributed to the state General Fund.

#### **Explanation of Local Expenditures:**

**Explanation of Local Revenues:** Because the increase in the civil service retirement deduction would serve to decrease taxable income, counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) could potentially experience a minimal decrease in revenue from these taxes.

**State Agencies Affected:** DOR.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** OFMA Income Tax Databases, 1996-2008; Lynn Wehner, Federal Office of Personnel Management.

**Fiscal Analyst:** Jessica Harmon, 317-232-9854.